States Tackle Foreclosures In Absence of Federal Help

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This month alone, Philadelphia's sheriff delayed foreclosure auctions of 759 homes at the city council's urging. Maryland extended the time it takes to complete a foreclosure. State leaders in Ohio recruited more than 1,000 lawyers to aid distressed borrowers.

Frustrated by the slow pace of federal action on behalf of struggling homeowners, some states and cities have struck out on their own to stem an alarming rise in foreclosures that has depressed home prices in most parts of the country and eroded local governments' revenues as property taxes and utility bills go unpaid.

Nine states have committed more than $450 million to "loan funds" aimed at refinancing the mortgages of at-risk borrowers, according to a study by the Pew Charitable Trusts. A handful have brokered deals with major lenders who have pledged to ease terms for some troubled loans. A few states have lengthened the time it takes to complete a foreclosure.

"What the states are saying is: 'We can't wait any longer for the federal government. We have to get ahead of this,' " said Tobi Walker, a senior officer at the Pew Charitable Trusts. "The states are experiencing this pain more directly than the federal government is."

Their efforts have yielded mixed results but underscore the pressure local lawmakers face. The number of homes entering foreclosure nationwide is the highest since the Mortgage Bankers Association started tracking the data in 1979. Nearly every state has been hit to some degree. New foreclosures climbed at least 20 percent in 47 states from December 2006 to December 2007, according to Pew.

In some ways, states and cities are better positioned to tackle the fallout than the federal government, housing experts said. They are more familiar with their communities and better able to tailor responses. Local governments lack the resources and clout, however, to effect large-scale change.

At the root of the problem are the lax lending standards that enabled borrowers with little money or poor credit to take out loans they could not afford when home prices shot up in the first half of the decade.

After the housing market softened in late 2005, an increasing number of borrowers could not sell their homes or refinance their way out of trouble. Mortgage default rates started rising.

Some states responded by creating loan funds they could use to refinance the most distressed borrowers. Pennsylvania created two new funds in November to cope with the recent mortgage problems.

One fund offers refinancing for troubled borrowers who have adjustable-rate loans if they meet certain criteria, including a cap on household income and limits on debt relative to income. These borrowers are offered cheaper, more predictable, 30-year fixed-rate mortgages.

The other fund is more aggressive, purchasing loans outright from lenders and then setting up affordable repayment plans with homeowners. In those cases, the agency works with lenders to reduce the mortgage's principal, instead of just rescheduling payments or temporarily reducing the interest rate.

Pennsylvania has refinanced 40 loans and negotiated principal reductions for an additional 38 under the two programs since they were adopted in November, said Brian Hudson, executive director of the state's Housing Finance Agency. In most cases, lenders have agreed to cut the principal by 15 to 30 percent.

"That is not a bad effort" for a few months of activity, Hudson said.

But loan funds have financial constraints. These funds can help only a limited number of borrowers, and even then they tend to have the greatest impact in states such as Pennsylvania that have not been overwhelmed by foreclosures.

They are less effective in previously overheated markets -- such as California, Florida and Nevada -- where borrowers grossly overpaid for their homes and now owe far more than their homes are worth, said Michael Collins of the PolicyLab Consulting Group, a mortgage research firm based in Ithaca, N.Y.

Through their own programs, New York has refinanced only three borrowers since September, and Massachusetts has refinanced 12 since July. These two loan refinancing initiatives do not help borrowers whose mortgages exceed the value of their homes.

"Once people are in that situation, there's not much that any state or local program can do unless the lenders make concessions," Collins said.

A few governors tried pushing lenders to do just that. California's Arnold Schwarzenegger attracted national attention in November when he announced that some of the state's largest lenders had voluntarily agreed to temporarily freeze interest rates on some adjustable loans.

The results have disappointed consumer advocates. The number of loan modifications, which could involve changing either the principal or interest rate of the mortgage, declined 30 percent from November to January while foreclosures climbed, said Paul Leonard, director of the Center for Responsible Lending's California office.

"These kinds of agreements are potentially very important but have not yielded the results people have hoped for," Leonard said. "That's the problem when you have bully pulpit negotiations as opposed to legislation."

For troubled borrowers in California, foreclosure remains the most common outcome, the California Reinvestment Coalition found after it surveyed 38 counseling firms in December that worked with 8,000 borrowers. Even some of the lenders that pledged to work with Schwarzenegger did not come through for borrowers, according to the coalition.

"We need something bigger and bolder, like some of the proposals in Congress," said Kevin Stein, the coalition's associate director.

Those proposals include providing $10 billion in new tax-exempt bonding authority for state and local housing agencies to refinance mortgages and $4 billion for cities to buy vacant foreclosed properties. Some proposals support expanding the role of the Federal Housing Administration so it can help refinance more troubled borrowers.

While the proposals wind their way through Congress, foreclosures keep mounting and local policymakers keep churning out ideas. An increasingly popular strategy is revamping the foreclosure laws in favor of borrowers.

Maryland has extended the timetable for foreclosure from 15 days to 150. Massachusetts has arranged temporary reprieves for more than 600 homeowners over the past year. Philadelphia is setting up a program that allows borrowers to get financial and legal counseling before auctions of their property are scheduled. The Ohio Supreme Court approved a mediation program in January.

Under the Ohio initiative, lenders who want to foreclose must first try to work out payments with homeowners. Only then will courts turn over the documents that companies need to sell the homes.

"That gives us leverage," said Richard Cordray, Ohio's treasurer. "To get what they need from our courts, they have to sit down and go through a mediation process as in all other civil cases. It slows down the process and gets everyone to the table."

In Ohio, manufacturing job losses have exacerbated the state's mortgage woes. Last year, more than 80,000 foreclosure cases were filed in Ohio courts, a 40 percent rise from four years ago. But that has not discouraged the state's relatively new leaders.

"I'm not at all pessimistic that we'll make a real dent in this problem," said Cordray, who took office a year ago. "It's just that we've got many bad loans to work through."